No. 13,503

IN THE

United States Court of Appeals

For the Ninth Circuit

GIULIO PARTICELLI, *Petitioner,* vs. COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	
ESTATE OF ELETTA PARTICELLI, Deceased, Arthur Guerrazzi, Executor, *Petitioner,* vs. COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	

On Review of The Tax Court of the United States.

PETITIONERS' REPLY BRIEF.

VALENTINE BROOKES,
ARTHUR H. KENT,
1720 Mills Tower, San Francisco 4, California,
Attorneys for Petitioners.

Subject Index

Table of Authorities Cited

No. 13,503

IN THE

United States Court of Appeals

For the Ninth Circuit

GIULIO PARTICELLI, *Petitioner,* vs. COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	
ESTATE OF ELETTA PARTICELLI, Deceased, Arthur Guerrazzi, Executor, *Petitioner,* vs. COMMISSIONER OF INTERNAL REVENUE, *Respondent.*	

On Review of The Tax Court of the United States.

PETITIONERS' REPLY BRIEF.

I. THE TAX COURT COMMITTED REVERSIBLE ERROR IN ADMITTING EVIDENCE TENDING TO SHOW THAT PETITIONER HAD PREVIOUSLY COMMITTED A CRIME.

In the most oblique fashion possible, respondent seems to admit error in the admission over petitioner's objection of evidence tending to establish that petitioner had previously committed a crime in selling wine at over-ceiling prices. As we demonstrated in our opening brief (pp. 16-17), if petitioner is understood to have testified that he at no time sold at over-ceiling prices he did so on cross-examination, and in that event respondent is bound by his testimony and it was error to permit him to impeach it. In his brief (p. 38, footn.), respondent states that the evidence to which we objected was offered "solely to rebut the taxpayer's testimony that he had never sold wine over the established OPA ceiling price." Since respondent cites no record reference to show that petitioner so testified on direct, and at the trial respondent's counsel admitted that if there was such testimony it was elicited on cross-examination (R. 527), he must mean to defend the ruling below on that factual assumption. Since under the cases his position cannot be defended (Pet. Op. Br. 15, 16-17), we do not see that any serious defense is offered.

Furthermore, respondent apparently seeks to create the impression that petitioner mistakenly objected to this evidence below on the ground it would open petitioner to criminal prosecution.[1] In the court below, respondent's counsel first thought when the objection was made that petitioner was claiming privilege against self-incrimination (R. 524), and candidly stated that his purpose was to impeach petitioner by proof of a crime (R. 524). Petitioner then objected to the offer for that or any purpose

---

[1] "not for the purpose of laying a foundation for the taxpayer's prosecution (R. 524, 528), as feared by the taxpayer (R. 524-525, 527-528)" (Resp. Br. 38, footn.).

(R. 525, 528).[2] Accordingly, the objection was properly preserved below.

Respondent also stated that "by his own admission" petitioner had made overceiling sales (Resp. Br. 38, footn.). This careless statement is entirely untrue. The record references cited by respondent are to the argument below of respondent's counsel, and not to testimony or other evidence. Respondent cannot point to evidence of such admissions, for there are none. See Petitioners' Opening Brief, p. 13, footnote.

Finally, and here respondent comes to the real point of his defense of the action below, respondent argues that no harm resulted from the error below, because the trial judge did not expressly admit that his refusal to credit petitioner was attributable to this impeaching evidence. This is not an acceptable defense. Prejudicial error cannot be permitted to go uncorrected merely because the trier of the facts refrained from admitting that he was prejudiced by it.

---

[2]Petitioner's counsel stated the objection in this way (R. 525): "if (this document) did prove what he is trying to prove it would, I repeat, be an effort to prove him guilty of a crime and thereby impeach his testimony."

Again, at R. 528: "Mr. Brookes: May I illustrate my point with a hypothetical case. Counsel might very well ask a question of a witness whether he had ever committed arson, and then an answer would naturally come out no, and then in this manner he would attempt to prove he had committed arson."

II. THE WRITTEN CONTRACT WAS NOT A SHAM AND PETITIONERS' TAX LIABILITY SHOULD BE DETERMINED ON THE BASIS OF ITS TERMS.

Respondent's position here is based on a series of contentions which can be speedily answered.

1. The contention that *Commissioner v. Court Holding Co.,* (1945) 324 U.S. 331, authorizes respondent to impose taxes on the basis of a psychoanalysis of the parties to a contract instead of on the basis of the terms of the contract[3] has been answered by our discussion at pages 38 to 42 of our opening brief. Essentially the same broad contention respondent makes here has recently been presented to and rejected by this Court in *Twin Oaks Co. v. Commissioner,* (CA 9, 1950) 183 F. 2d 385, and *Hypotheek Land Co. v. Commissioner,* (CA 9, 1953) 200 F. 2d 390.

2. This case has provided respondent with another opportunity to urge his favorite contentions: (a) what the taxpayer did was prompted by tax saving considerations; (b) any action so motivated cannot be given effect. Both contentions are baseless.

(a) To argue on this record that the contract took the form it did in order to reduce petitioner's taxes is ridiculous. The Tax Court did not so find, and we suggest that the Tax Court would not have neglected to make such a finding had it thought the evidence would have supported it. The record is replete with the evidence of what motivated the parties—desire to conform to what

---

[3]Respondent does attempt an argument based on the terms of the contract. At p. 30 of his brief he attempts to convert the "time clause" in the contract into the contract itself. Extended argument is not needed to establish that a clause fixing time for performance does not override the allocation clauses in a contract.

they understood were the regulations of the Office of Price Administration. The only record references respondent cites for his assertion that petitioner caused the contract to take the form it did in order to reduce his taxes are pp. 272-274 (Resp. Br. 27). These references are to the cross-examination of Mr. George E. Oefinger, C.P.A., a partner in the noted national accounting firm of Arthur Andersen & Co. (R. 277). Previously Mr. Oefinger had testified that he had advised petitioner that he must observe the ceiling price in this sale and that he could not sell the wine for a price in excess of 28 cents a gallon (R. 264, 265). Mr. Oefinger's testimony is well summarized in his own words (R. 264-265):

> "A. Well, his primary concern was about the sale of the wine. In other words, he realized, as I had told him before and I think he knew of his own knowledge, that there was a ceiling price that had been established by the OPA on the sale of wine, and he knew because I had so informed him that if any wine was sold in bulk in excess of that—of that ceiling price, he was subject to penalties which might go as high as three times the difference between the price at which it might be sold and the ceiling price.
>
> "Q. When he brought these parties to your office, did he consult you then about the ceiling price?
>
> "A. Yes, he did. As a matter of fact, he asked me to make a determination as to what the ceiling price would be in this particular instance, which I proceeded to do.
>
> "Q. What did you tell him was the ceiling price?
>
> "A. I told him after I completed the computation. I told him in my judgment the ceiling price for that wine was not in excess of 28 cents a gallon."

Since this testimony, unless rebutted or shaken, would completely eliminate any serious contention that tax-saving motives dictated the form of the contract, respondent's trial counsel on cross-examination tried to, but could not, shake Mr. Oefinger. The witness admitted that he had advised petitioner of the tax consequences of the transaction (R. 274), but adhered to his previous testimony that the 28-cent a gallon price for the wine was used because it was the ceiling price (R. 274-276). He even produced his work papers on which he had, at the time, made his calculations of the ceiling price (R. 274-275).

Elsewhere in the brief (Resp. Br. 22) respondent states that the "obvious reason" the figures were "juggled" to be consistent with the ceiling price on wine was for tax avoidance. We submit such a statement does not rise to the dignity of argument. The Court cannot, and should not be asked to, take judicial notice that all transactions are framed for tax avoidance. In the absence of supporting evidence, as in the case here, that is precisely what respondent is asking this Court to do.

(b) Transactions beween unrelated parties, dealing at arm's length, cannot be set aside merely because motivated in part by tax avoidance. Only if the contract is sham may it be ignored. *U. S. v. Cumberland Public Service Co.,* (1950) 338 U.S. 451; *Goold v. Commissioner,* (CA 9, 1950) 182 F. 2d 573, 575; *Twin Oaks Co. v. Commissioner,* (CA 9, 1950) 183 F. 2d 385; *Hypotheek Land Co. v. Commissioner,* (CA 9, 1953) 200 F. 2d 390.

Accordingly, the tax avoidance motive, even if shown by the evidence to exist, would not support the decision below.

3. (a) Apparently respondent recognizes that there is too much conduct consistent with the terms of the contract for him to be able to argue successfully that the contract was a sham. Accordingly he argues that the price allocation in it can be disregarded because, unlike the rest of the contract, it was "self-serving" (Resp. Br. 16). He specifically admits (Resp. Br. 28) that the negotiations were at arm's length so far as the total price was concerned, but contends that the allocation provisions in this arm's length contract were "self-serving," notwithstanding they were signed and agreed to by the unrelated, independent purchaser.

The conception is a startling one. It is an admission that respondent contends he has an inherent power (no statutory provision is relied on to confer it) to analyze every arm's length sale to see if both sides have an equal interest in every detail of it and if they have not, he can substitute his terms for those of the parties. The newspapers have recently carried stories of the sale, subject to stockholders' approval, of all the assets of Willys-Overland Motors, Inc. to Kaiser-Fraser Corporation. Apparently respondent conceives his powers to be such that if he can find that Kaiser-Fraser Corporation did not want to buy all the Willys assets but had to take all in order to acquire those it wanted, the Commissioner of Internal Revenue can rewrite the contract to substitute his own allocation of the total price to different assets for the allocation made by the parties. Is it not abundantly clear (1) that this is a new power for which respondent is grasping, and (2) if he can do what he is seeking to do here he can do it in the Willys-Kaiser-Fraser case?

And while we are on the subject of actions motivated only by tax considerations, does anyone suppose respondent's allocation, if he is free to make it, will be *free* of tax considerations?

(b) In any event, assuming respondent can divide an arm's length contract into "arm's length" portions and "self-serving" portions, his contention that Tiara had no interest in the allocation is unrealistic and contrary to demonstrable fact.

Tiara entered the wine cost on its books at $77,000. Because it used this figure as the cost of the wine, if Tiara sold the wine for $2.00 a gallon net to it,[4] there would be a taxable profit of $1.72 a gallon. Since the World War II excess profits tax reached a rate of 90%, Tiara could be liable for income and excess profits taxes of $1.55 on each gallon sold. This tax, respondent says, was of no significance to Tiara, so it willingly agreed to the 28-cent allocation as a favor to petitioner.

In cognizance of the fact that it is obvious that this tax would be important to anyone, including Tiara, respondent's theory proceeds from here: respondent says that this tax was unimportant to Tiara because by selling the winery Tiara could establish a tax loss under Sec. 117(b) [Resp. Br. 26, 44]. Since Sec. 117(b) provides

[4]Victor Dumbra testified Tiara could get this price by bottling the wine (R. 599-600, 620).

for capital losses, which corporations cannot deduct from ordinary business income, we do not see where Sec. 117(b) could have been helpful to Tiara.

In any event, we submit that respondent's theory why the contract figures made no difference to Tiara is far-fetched and artificial. Respondent's theory places Tiara in the position where it had to sell the winery in 1944 in order to establish a loss to offset its wine profit.[5] We find it impossible to believe that Tiara or any other buyer would *lightly* place itself in such a position. To contract itself deliberately into a position where it had to make a forced sale of the winery in 1944 to establish a tax loss was a serious matter indeed, and not, as respondent urges, a thing of indifference to Tiara.

4. (a) Respondent seeks to support the trial court's failure to give effect to petitioner's testimony that the 1,000 gallons of wine petitioner retained were high-grade wine and not wine of his own manufacture by pointing to cases involving the power of the trier of the fact to reject contradicted or improbable testimony. This testimony was, however, not contradicted by anything in the record: it may be noted that respondent's trial counsel did not even try to contradict it. For instance, the Dumbra brothers, who were respondent's witnesses, were

[5]This assumes Tiara intended when it bought the winery to sell it in 1944. This assumption is factually incorrect. Tiara would have retained the winery and used it but for the then unforeseen fact that subsequently Tiara bought a larger and better equipped winery. Victor Dumbra specifically so testified. (R. 602, 605.) After all, this is the winery in which petitioner made this wine on which respondent contends he made a profit of 50 cents a gallon, a 100 per cent profit!

not examined about the character of this wine, and since they were his witnesses respondent's trial counsel may be presumed to have known what their testimony on this point would have been had they been asked for any. Petitioner's testimony is also not improbable. He regularly sold, in his retail store, wine purchased from better vintners than he, including Italian Swiss Colony, to whom he attributed the wine under discussion. It is not improbable that he had some on hand, and any vintner would have known enough to reserve it instead of petitioner's own vintage which, being but partially finished, would not keep. The importance of the wine's ability to keep is shown by the fact that when this case was tried, over six year after the fact, petitioner still had some of the wine on hand. (R. 217, cf. R. 132.)

Respondent seeks to find a contradiction in the fact that petitioner elsewhere testified that all the wine sold to Tiara was of his own vintage. There is no contradiction here. It was understood by the parties when the sale was made that petitioner was to retain this wine, not sell it to Tiara. Petitioner so testified (R. 132):

> "* * * I reserved the right to take some wine when I sold the winery and wine to Mr. Dumbra."

Respondent's own evidence (Exhibit L) is to the same effect. It says, in part (see Pet. Op. Br. p. 31):

> "You will recall that 1,000 gallons were withdrawn by Mr. Particelli *prior to the closing of the deal* and that *the whole deal amounted to 274,000 gallons,* with an adjustment to be made by Particelli in connection with the 1,000 gallons." (Emphasis ours.)

Accordingly, the 274,000 gallons actually sold were of petitioner's own vintage, and testimony to that effect does not contradict his further testimony that the 1,000 gallons not intended to be sold to Tiara were Italian Swiss Colony wine.

(b) Respondent also relies (Resp. Br. 33, footn. 10) on testimony of one Alberigi that petitioner had told him that he had sold 400,000 gallons of wine for $1 a gallon and had thrown the winery in to make it legal. The real significance of Alberigi's testimony is its contradiction of petitioner's tax avoidance theory.

Petitioner's statement to Alberigi, if actually made,[6] was such plain braggadocio that it is incredible to us that anyone should be asked to believe it in preference to testimony given under oath. Moreover, on its face this braggadocio was false. Petitioner did not sell 400,000 gallons of wine. He did not give the winery away for nothing. He did not receive $400,000 for anything. Even respondent has never allocated the entire consideration to the wine, or based his deficiency on a $400,000 sales price. Of what probative effect, then, is the remaining portion of this hearsay, to the effect that petitioner sold his wine for $1 a gallon? None, we submit. It was merely the idle crackerbarrel chatter of a vintner understandably unwilling to admit, when not under oath, that he had been forced by the ceiling prices to sell his wine for less than his grape costs.

---

[6]Which petitioner did not recall having made and did not believe he had made (R. 373). Again, however, the trial court discredited petitioner and found the statement was made. This is further proof of the seriousness of the improperly received impeaching evidence.

(c) No argument we have made is made in reliance on any evidence which is contradicted by anything in the record. Our arguments for reversal are based entirely on uncontradicted evidence and the findings of the Tax Court. Accordingly, we ask nothing of this Court which it may not properly accord us under the cases cited by respondent.

III. THE MARKET VALUE OF THE WINE DID NOT EXCEED 28 CENTS A GALLON, AND IT WAS ERROR TO ALLOCATE A HIGHER PRICE TO IT.

Respondent has evidently been unable to answer our point (Pet. Op. Br. 45) that the expert witnesses' testimony of value[7] was based solely on franchise bottling sales, a type of grey market of which the parties here had no knowledge. In any event, respondent has not attempted to answer it.

Neither has respondent replied to our contention (Pet. Op. Br. 53-54) that petitioner's sale was subject to the ceiling because, to avoid it, there must have been a sale of the entire business, which here there was not. Instead, respondent has said (Resp. Br. 39) that "admittedly" there was no ceiling applicable to the sale. We suppose respondent means that *he* "admits" it, for our opening brief made it abundantly clear that we do not. Instead,

---

[7]Respondent has erroneously (Resp. Br. 37) stated that the range of value they testified to was 75¢ to $1.25 a gallon. The record references respondent cites show that Mondavi testified that the value ranged from 75¢ to $1.00 a gallon, and Gomberg valued the wine at $1.00 a gallon. While Gomberg said there had been some franchise bottling sales at $1.25 a gallon (R. 459), his opinion valued the wine at $1.00 a gallon (R. 458).

we have shown, we submit, that this sale was not within the narrow exemption the OPA rulings opened up.

Perhaps our advocacy has distorted our perspective, but we believe this case presents a strange spectacle! Here the Government, through its Department of Justice, is in court arguing that its seriously meant and earnestly executed efforts to impose wartime price ceilings on goods were so ineffective that there was, to quote, "a free open market"[8] in wine, which established the fair market value of the wine in preference to its ceiling price. If the Government displays such a cynical view of its laws and regulations, how can citizens do otherwise? We wonder if victory in a tax case should be won by such measures, and if it can be worth the price.

Furthermore, respondent's discussion of the effect of ceiling prices on market values proceeds as if he had read neither our brief nor the cases on the point. Thus, after referring to the Supreme Court cases on the point, he asserts (Resp. Br. 40):

> "* * * the Court had no occasion to determine and made no determination at all that the ceiling price constituted the fair market value under the unusual facts of those cases."

This is respondent's statement. But the Supreme Court said (*United States v. Commodities Trading Corp.* (1950) 339 U.S. 121, 124):

> "Thus ceiling prices of commodities held for sale represented not only *market value* but in fact the only value that could be realized by *most* owners.

---

[8]Resp. Br. 37; semble, Resp. Br. 24.

> Under these circumstances they cannot properly be ignored in deciding what is just compensation." (Emphasis added.)[9]

Again, in the same opinion, the Supreme Court said (339 U.S. 129):

> "* * * *The general rule has been that the Government pays current market value for property taken, the price which could be obtained in a negotiated sale, whether the property had cost the owner more or less than that price.* (Citation omitted.) The reasons underlying the rule in cases where no Government-controlled prices are involved also support its application *where value is measured by a ceiling price.*" (Emphasis added.)[10]

The foregoing quotations need no explanation. They need only to be read. They establish that the Supreme Court has indeed held that ceiling prices establish the fair market value.

Respondent also argues (Resp. Br. 40):

> "Here the ceiling price was substantially less than the cost, and therefore it may not be presumed, under the particular facts here, that the ceiling price of 28¢ a gallon would under any circumstances be determined to be just compensation in the event of requisition by the Government * * *."

The Supreme Court has held to the complete contrary of what respondent argues. Accepting the contentions of the Solicitor General, that Court has held that even where

---

[9]Quoted at p. 51, Petitioners' Opening Brief.
[10]Quoted at p. 52, Petitioners' Opening Brief.

it was less than cost to the owner, ceiling price fixed the condemnation price. In the *Commodities Trading* case, the Supreme Court said (339 U.S. at 129):

> "Another contention is that the particular pepper turned over to the Government cost Commodities more than the ceiling price, and that this is a special circumstance sufficient to preclude use of the ceiling price here. * * * we think that the cost of the pepper delivered provides no sufficient basis for specially excluding Commodities from application of the ceiling price."[11]

The Supreme Court held that pepper which cost the citizen 12.7 cents a pound could be requisitioned by the United States for 6.63 cents a pound solely because the latter was the ceiling price. All this we previously stated in our opening brief at pp. 50-52. It is obvious that the 50 cents a gallon cost of petitioner's wine would have been accorded no more significance than the 12.7 cents a pound cost of Commodities' pepper, and we suggest that respondent would have shown this Court the respect due it had he candidly admitted that this point is a settled one and is not open for debate.

CONCLUSION.

The crux of respondent's case is his complaint that petitioner sold his wine at the ceiling price. Entirely apart from the questions of public policy raised by such a complaint's emanating from an agency of the Govern-

---

[11]Quoted at p. 52, Petitioners' Opening Brief.

ment, we submit that respondent has actually confused his real complaint. He is really complaining because petitioner sold his winery for $273,000. Petitioner could not lawfully have sold his wine for more than $77,000, and had he sold only his wine he would have reported a loss for the year 1943 and paid no tax at all. As it is, he made a large capital gain and paid a large tax solely because he was able to and did sell his winery for a large profit. Thus the fisc benefited from petitioner's sale of his winery; it received more taxes than if petitioner had sold his wine at ceiling and retained his winery. We submit respondent should not be heard to complain.

For the error at the trial, a new trial is the only remedy if respondent has sufficient case on the merits to warrant the expense of a retrial. We submit respondent has not. The judgment below should be reversed and judgment entered for petitioners on the points raised in this appeal.

Dated, San Francisco, California,
April 17, 1953.

Respectfully submitted,
VALENTINE BROOKES,
ARTHUR H. KENT,
Attorneys for Petitioners.